

Message Text

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ACTION EB-04

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FM AMEMBASSY MADRID

TO SECSTATE WASHDC IMMEDIATE 9053

C O N F I D E N T I A L SECTION 1 OF 2 MADRID 1341

LIMDIS/GREENBACK

E.O. 11652: GDS

TAGS: EFIN, ECON, SP

SUBJECT: VIEWS OF PRESIDENCY ECONOMIC PLANNING OFFICIALS ON
CURRENT SPANISH ECONOMIC SITUATION AND APPROPRIATE MEASURES

REF: MADRID 1145, 1146, 1298

1. SUMMARY. UNDER SECRETARY OF THE PRESIDENCY FOR PLANNING RICARDO CALLE AND MEMBERS OF HIS STAFF ON FEBRUARY 17 GAVE DCM AND EMBASSY OFFICERS VIEWS ON THE ECONOMIC SITUATION AND A PREVIEW OF LIKELY GOS ACTIONS THAT TENDED TO CONFIRM PAST IMPRESSIONS OF LACK OF STRONG LEADERSHIP WITHIN THE GOVERNMENT ON ECONOMIC MATTERS AND OF THE LIKELIHOOD OF CONTINUED TEMPORIZING AT LEAST THROUGH ELECTIONS. SOME POSITIVE MEASURES MAY BE TAKEN IF CALLE'S PREDICTIONS ARE RIGHT, BUT THERE WILL BE NO COHERENT OVERALL PROGRAM IN THIS PERIOD AND PERHAPS EVEN SOON AFTER ELECTIONS THAT WILL FACE UP TO THE TWIN PROBLEMS OF A 20 PERCENT OR HIGHER INFLATION RATE AND A SEVERE BALANCE OF PAYMENTS DEFICIT FOR WHICH FINANCING WILL BECOME INCREASINGLY PROBLEMATIC. WHAT CALLE AND HIS COLLEAGUES HAD TO SAY MUST BE QUALIFIED, OF COURSE, BY HOW EFFECTIVE OTHER ACTORS ON THE SCENE MAY BE IN PRESSING THEIR VIEWS, AND BY THE EFFECT THAT OBJECTIVE ECONOMIC DEVELOPMENTS MAY HAVE. END SUMMARY.

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2. WE HAVE BEEN TOLD THAT THE UNDER SECRETARIAT OF PLANNING FOR THE PRESIDENCY, NOT THE MINISTRY OF FINANCE, THE BANK OF SPAIN, OR OTHER ECONOMIC MINISTRIES, IS NOW THE KEY OFFICE WITHIN THE GOS ON OVERALL ECONOMIC AND FINANCIAL POLICY. IF THAT IS INDEED THE CASE, EMBASSY OFFICERS WERE GIVEN A FURTHER DEMONSTRATION OF THE GOS LACK OF STRONG

ECONOMIC LEADERSHIP IN A CONVERSATION ON FEBRUARY 17 WITH UNDER SECRETARY OF PLANNING CALLE AND TWO OF HIS SENIOR STAFF. CALLE AND HIS COLLEAGUES ARE ENERGETIC AND HARD-WORKING, BUT ARE BASICALLY STILL STUDENTS OF THE GAME THEY ARE PLAYING IN, SEEM TO LACK A REALISTIC OVERALL VIEW OF WHAT IS NEEDED, HAVE HAD A HARD TIME GETTING TIMELY TOP-LEVEL ATTENTION, AND APPARENTLY ALSO HAVE BEEN BEATEN DOWN ON SOME OF THEIR SOUNDER IDEAS. CALLE SAYS THAT THE ECONOMIC MEASURES THAT PROBABLY WILL BE ADOPTED BY THE COUNCIL OF MINISTERS ON FEBRUARY 18 WERE PROPOSED IN THEIR FIRST VERSION TO PRESIDENT SUAREZ BY HIM IN EARLY NOVEMBER. SUAREZ THANKED HIM FOR THEM IN EARLY DECEMBER BUT THEY HAVE SINCE GONE THROUGH SOME 30 DRAFTS AS THE RESULT OF INTER-MINISTERIAL DISCUSSION. CALLE HIMSELF JOINS IN AT CABINET-LEVEL DISCUSSIONS OF ECONOMIC MATTERS, AS A TECHNICAL EXPERT. BUT HE DOES NOT HAVE MINISTERIAL RANK, AND HIS STAFF IS NOT AS TECHNICALLY COMPETENT AS THE TOP STAFF OF BANK OF SPAIN (WHOSE GOVERNOR IS NOT PRESENT FOR CABINET DISCUSSIONS) NOR DOES HIS STAFF HAVE THE IMMEDIATE DIRECT ACCESS TO SOME OF THE DATA THAT THE MINISTRY OF FINANCE AND BANK OF SPAIN HAVE. CALLE CONFIRMED THAT PRIME MINISTER SUAREZ HAD PLANNED TO APPOINT A MINISTER OF THE PRESIDENCY WITH OVERALL ECONOMIC COORDINATING POWERS, BUT NOTHING HAS BEEN HEARD OF THIS IDEA RECENTLY.

3. CALLE STATES THE MEDIUM-TERM PROGRAMS THAT HE AND HIS STAFF ARE PRESENTING TO THE GOVERNMENT HAS TWO PILLARS: (A) MAINTENANCE OF THE MARKET ECONOMY, AND (B) STRENGTHENING OF THE PUBLIC SECTOR. SOME OF THE SPECIFIC MEASURES BEING PROPOSED SHOULD

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INDEED BY CONSTRUCTIVE TOWARD THESE ENDS; OTHERS WILL HAVE LITTLE EFFECT; AND THERE IS CLEAR LACK OF A COHERENT, RESPONSIBLE OVERALL PROGRAM.

4. CONSTRUCTIVE PROPOSALS INCLUDE MORE RATIONAL, HIGHER ENERGY PRICES; PROGRESSIVE FREEING OF INTEREST RATES THROUGH 1977; AND COMMITMENT TO BASIC TAX REFORM (BUT TO BE ACHIEVED ONLY OVER A TWO-YEAR PERIOD). THERE IS ALSO A PROPOSAL, WHICH MAY OR MAY NOT PROSPER, TO GIVE BUSINESS GREATER FLEXIBILITY IN DISMISSING UP TO 5 PERCENT OF ITS LABOR FORCE, BUT ONLY AFTER TAX REFORM HAS BEEN IMPLEMENTED.

5. PROPOSALS LIKELY TO HAVE LITTLE EFFECT, UNLESS MORE FUNDAMENTAL PROBLEMS ARE ADDRESSED, ARE INCREASED DIRECTED CREDIT FOR EXPORTS AND SMALL AND MEDIUM INDUSTRY, AND A MODEST INCREASE IN PUBLIC SECTOR INVESTMENT. (WITH REGARD TO THE BUDGET, CALLE EXPLAINED THE ANOMALY OF THE APPARENT DISAPPEARANCE OF THE 1976 PUBLIC SECTOR DEFICIT (MADRID 1146) BY SAYING THAT MINISTER OF FINANCE CARRILES HAD A

FIXATION ON BUDGET BALANCE AND SIMPLY HAD NOT PERMITTED MINISTRIES TO SPEND MONIES ALREADY ALLOCATED TO THEM. HE ALSO IMPLIED THAT THE PUBLIC SECTOR BUDGET HAD BEEN "BALANCED" BY CONSIDERABLE FOREIGN BORROWING, AND SAID THAT HE WAS RECOMMENDING FURTHER FOREIGN BORROWING TO FINANCE THE PROPOSED INCREASED INVESTMENT EXPENDITURES.)

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C O N F I D E N T I A L SECTION 2 OF 2 MADRID 1341

LIMDIS/GREENBACK

6. BASIC ISSUES NOT ADDRESSED ARE OVERALL MONETARY POLICY AND THE EXCHANGE RATE. CALLE IS ACCEPTING THE ARGUMENT OF OTHERS FOR A CONTINUATION OF EXPANSION OF MONEY SUPPLY AT THE PREMISSIVE RATE OF 21 PERCENT ON THE THESIS THAT A MORE RESTRICTIVE MONETARY POLICY WOULD HAVE INTOLERABLE COSTS IN TERMS OF GREATER UNEMPLOYMENT AND BUSINESS FAILURES. ON THE EXCHANGE RATE, HE PROPOSED LAST OCTOBER THE INITIATION OF A POLICY OF PROGRESSIVE DOWNWARD FLOAT, BUT WAS TURNED DOWN. HE NOW ARGUES THAT NOTHING NOW CAN OR SHOULD BE DONE IN TERMS OF EXCHANGE RATE ACTION BEFORE ELECTIONS AND PERHAPS EVEN FOR SOME TIME AFTERWARDS. WHILE SOME OF HIS STAFF ARGUE THAT A DEVALUATION MAY BE SIMPLY BE FORCED BY EVENTS IN THE MARKET, HE SEEMS AT THIS TIME TO BE DEFENDING A GOVERNMENT THESIS THAT NEITHER MONETARY RESTRAINT NOR EXCHANGE RATE CORRECTION IS POSSIBLE OR EVEN DESIRABLE NOW. THE FURTHER ARGUMENT SEEMS TO BE, IN EFFECT, THAT FOREIGN OFFICIAL AND PRIVATE CREDITORS SHOULD UNDERSTAND AND SUPPORT INFLATIONARY SPANISH ECONOMY WITH A PEGGED OR ONLY SLIGHTLY MOVING EXCHANGE RATE UNTIL SPAIN SOMEHOW WORKS ITSELF OUT OF ITS PROBLEMS. MEANWHILE, 50 PERCENT ADVANCE IMPORT DEPOSITS ARE BEING PROPOSED BY THE MINISTER OF INDUSTRY. THE PRESIDENCY PLANNING OFFICE IS OPPOSING THIS MOVE BUT MAY NOT WIN.

7. EMBASSY OFFICERS ASKED CALLE WHETHER HE WOULD BE HAVING
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CONTACT WITH THE IMF ANNUAL CONSULTATION TEAM DURING ITS
CURRENT VISIT HERE. CALLE SAID HE EXPECTED THERE WOULD BE
SUCH CONTACTS, BUT DID NOT SEEM DEFINITE. EMBASSY OFFICERS
SAID THEY THOUGHT SUCH CONTACT, AND OTHER CONTACTS WITH THE
TEAM AT AS HIGH A LEVEL AS POSSIBLE, WOULD BE USEFUL, PAR-
TICULARLY IN VIEW OF THE ROLE THE IMF DOUBTLESS WOULD
EVENTUALLY PLAY IN CREDIT ARRANGEMENTS FOR SPAIN. CALLE THEN
SAID HE EXPECTED THAT, IN ADDITION TO PLANNING, THE BANK OF
SPAIN AND WORKING-LEVEL MINISTRY OF FINANCE OFFICIALS, THE
MINISTER OF FINANCE AND VICE PRESIDENT OSORIO WOULD SEE
THE IMF TEAM DURING ITS VISIT.

8. COMMENT: PRIME MINISTER SUAREZ MAY NOT BE SO ISOLATED
FROM SOUND OVERALL ADVICE ON THE ECONOMY AS OUR CONTACTS
WITHIN THE GOVERNMENT THUS FAR INDICATE. SOME OF OUR BANK-
ING AND BUSINESS CONTACTS HAVE TOLD US THEY HAVE GIVEN HIM
AND OTHER TOP GOS OFFICIALS QUITE DIFFERENT RECOMMENDATIONS THAN
THOSE OUTLINED BY CALLE. BUT THE GENERAL DIRECTION OF THE GOVER-
NMENT'S COURSE ON ECONOMIC MATTERS SEEMS CURRENTLY ROUGHLY ALONG
THE LINES CALLE AND HIS COLLEAGUES INDICATED TO US. THIS ONLY
UNDERLINES THE IMPORTANCE OF COUNSEL FROM THE IMF AND OTHER
COMPETENT SOURCES WITH STATURE SUCH THAT THEY WILL BE HEARD.
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